BEFORE THE FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE
PUBLIC MEETING ON UNIVERSAL SERVICE PORTABILITY AND ELIGIBLE TELECOMMUNICATIONS CARRIER DESIGNATION PROCESS
DENVER, COLORADO
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PANEL 1: BASIS OF SUPPORT

In Alaska, the home of the most competitive wireline local markets in the country, GCI is at the forefront of national universal service policy issues, and we offer our experiences as a window into the near future for other developing competitive markets throughout the country. The universal service fund is an essential component of national telecommunications policy, and the focus should remain on improving service to consumers, not on particular carriers. GCI believes that competitively neutral policies will further the goals of universal service by enhancing efficiency and encouraging the development and deployment of new services in high-cost areas. Competition is necessary to discipline carriers and incent them to provide service in a cost-effective manner, and if allowed to work, will help ensure that the universal service fund cost structure does not grow so large that it becomes impossible to sustain.

The same amount of per-line support should be available to competitive eligible telecommunications carriers (CETCs) as for incumbent local exchange carriers (ILECs). Supporting rate-of-return ILECs based on ILEC embedded costs and CETCs based on CETC costs would fail to provide equal opportunity for support, prevent the market from

working as it would without subsidies, and lead to unnecessary USF fund growth. Differential support for ILECs and CETCs poses two primary problems: first, it masks the ability to discover the smallest necessary subsidy through competition, and second, it presents an administrative morass. Therefore, the optimal outcome remains issuing the same amount of per-line support to CETCs and ILECs. GCI does not oppose determining support for both ILECs and CETCs based on CETC per-line costs, ILEC per-line costs, or based on a model. The key is that the support payment—however it is determined—must be the same for all market participants.

USF support should not be used to dampen competitive signals. The inherent inefficiencies and competitive biases created by a system that pays differential support to ETCs in the same market may be illustrated by considering how that market would function in the absence of support payments. For example, ACS of Fairbanks (ACS-F) today receives lump-sum monthly high cost support roughly equivalent to $12.17 per line per month for serving residential customers in Zone 2 of the ACS-F study area. GCI also receives $12.17 per line per month for serving lines in the same area.

In the absence of this subsidy, ACS-F retail rates would need to be approximately $12.17 per line per month higher for ACS-F to receive the same revenue it now receives, and GCI would have the opportunity to compete for that entire $12.17 for every customer. GCI would have the incentive to enter based on the unsubsidized amount of revenue it would receive in competition with ACS-F unsubsidized prices. If GCI were 10 percent more efficient than ACS, it would have the option of cutting its rates by up to 10 percent to attract more customers. Over time, basic economics predicts that competition will move prices toward the long run incremental costs of the most efficient provider.

Providing an equal support amount to both ETCs simply reduces the customers' price by $12.17, while maintaining the same revenue opportunity for each ETC and transmitting the same pricing signals and efficiency incentives to both carriers.

By contrast, competitive incentives and market discipline would be greatly skewed if a subsidy were provided to only one ETC but not another, or in a greater amount to one ETC than to another—regardless of whether the greater amount is issued to the CETC or the ILEC. If the ILEC receives a subsidy, but the CETC receives no subsidy for providing essentially the same service to the same subscriber, the CETC would have no incentive to enter unless it could provide lines at an average of the subsidy amount (or the difference between subsidy amounts) *less* than the ILEC. Under this system—the system that would result if CETC support differed from ILEC support—the competitive market's incentives for efficient service would be blunted dramatically, and the ratepayer would fund inefficient service through universal service fees. And the ability to incent higher quality services to consumers and discipline fund demand through competition will be lost. The Joint Board and the Commission already got this right. Unequal support cannot be competitively neutral and will skew the market in favor of the ILEC.

Claims that providing support to CETCs gives preferential treatment or provides a windfall to CETCs are incorrect. The CETC and ILEC costs may be different, but all carriers are subject to the requirements of Section 254(e), which provides that support may only be used "for the provision, maintenance, and upgrading of facilities and services for which the support is intended." State commissions are in the best position to determine compliance with this requirement when they certify ETC support on an annual

basis. Likewise, calculating high cost support for CETCs using UNEs on a basis other than ILEC support would also be inefficient and discriminatory by providing ILECs with an unwarranted universal service-based advantage. Today, the Commission's rules providing for geographic UNE rate deaveraging and high cost disaggregation already address any potential for artificial "windfalls" to CETCs using UNEs (in whole or in part) to provide supported services.

Differential support would also completely eliminate any incentive for cost cutting by either carrier. Both ILECs and CETCs would essentially be under parallel, but non-interacting, systems of rate-of-return regulation. As each carrier increases its costs, its support and thereafter, total revenue per unit (but not the price on which it competes to win customers) would increase. The more each carrier increases its costs, the more support it would receive. The result would be to infuse CETCs with the same poor incentives as ILECs under rate-of-return regulation—increase costs to maximize support. At the same time, competition can no longer be employed to lead to more efficient pricing, share cost reductions with consumers, and reveal the need for lower subsidy amounts to maintain affordable rates.

Assessing CETC support based on individual carrier costs also poses a regulatory morass. To prevent an unchecked upward climb in support, full rate-of-return regulation of CETC rates would have to be instituted. CETCs, which generally are neither incumbent nor dominant carriers, have not been subject to the panoply of cost accounting and regulatory requirements that apply to ILECs. There is no common accounting system or categories to reach comparative results, and there has been no need or interest in extending such requirements to competitive carriers. In addition, CETCs and ILECs

typically do not share the same network topology or geographic scope. As result, regulations would be required for determining what constitutes a loop when, for example, the ILEC has five switches in the market and the CETC has one, or in some cases, none. Also, allocation rules would have to be devised for determining how to divide costs among shared facilities. Neither self-certification nor "average schedule" costs for CETCs avoid these issues, because the threshold determination of how costs will be calculated must be made to have a workable, enforceable, predictable system of support.

Finally—and perhaps most importantly—the question must be asked what will be achieved by calculating CETC USF support on CETCs' own costs? It certainly cannot be assumed that fund demand will decrease, as both ILECs and CETCs will have the incentive to maximize support. In addition, the proposal overlooks an existing inequity in the fund—that CETCs receive support on a per-line basis while ILECs receive support for their network costs, regardless of the loss of lines to competition. While ILEC proposals to calculate CETC support appear to be based on the assumption that CETC network costs will be lower, that assumption may not prove to be true in the early years of a new competitive entrant with a small customer base. Paying for the CETCs entire network and doing so in the early years of service could *increase* support to CETCs and increase fund demand.

The best option remains equal per-line support for CETCs and ILECs. This result precludes the need to impose rate-of-return regulation and incumbent network conventions on non-regulated carriers. It avoids the need for investigating CETC cost declarations. It also avoids the possibly unintended consequence of creating an increase in overall support, which may be driven by payment from USF of CETC network costs.

Finally, equal per-line support preserves the same competitive dynamics as would exist in the absence of USF support payments. As a result, competitively neutral universal service support will work to keep in check demands for full, perpetual recovery of self-reported ILEC costs and to ensure the development and delivery of services that are reasonably comparable in price and quality throughout all regions.